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Supreme Court of the United States

OCTOBER TERM, 1979

No. 78-1201

MOBIL OIL CORPORATION,

Appellant,

—VS.—

COMMISSIONER OF TAXES OF VERMONT,

Appellee.

ON APPEAL FROM THE SUPREME COURT OF VERMONT

APPELLEE'S BRIEF

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Statement of the Case

I. *The Vermont Law*

Vermont imposes an annual net income tax on every taxable corporation.[1] Vermont net income is defined as taxable income

[1] 32 V.S.A. §5811(15) defines a taxable corporation as ". . . for any taxable year, a corporation which, at any time during that taxable year:

(A) Was incorporated under the laws of this state;

(B) Possessed a certificate of authority to do business within this state; or

(C) Received any income allocable or apportionable to this state under the provisions of section 5833 of this title."

During the years in question, Mobil possessed a certificate of authority to do business in Vermont. In addition, Mobil received income, owned property, paid wages and made sales within Vermont and, accordingly, received income allocable to Vermont under §5833.

under the laws of the United States.[2] If income is derived from business activities both within and without Vermont, then the 6-percent Vermont tax is imposed only on net income apportioned to fairly and equitably represent the extent of business activities in the State. Under Vermont's apportionment formula, a multistate corporation's net income apportioned to Vermont is based on the arithmetic average of the percentages of its total payroll, property and sales attributable to its business activities in Vermont.[3]

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[2] 32 V.S.A. §5811(18) defines Vermont net income as ". . . for any taxable year and for any corporate taxpayer, the taxable income of the taxpayer for that taxable year under the laws of the United States, excluding income which under the laws of the United States is exempt from taxation by the states." It should be noted that the description "Vermont net income" is misleading in that it defines net income, before apportionment to represent business activities in Vermont. By incorporating, without modification, taxable income under the laws of the United States as Vermont net income, before apportionment, Vermont excludes all federal, state and foreign taxes claimed as deductions for federal income tax purposes.

Taxable income under the laws of the United States is incorporated by reference:

". . . to conform the Vermont . . . corporate income taxes with the United States Internal Revenue Code, except as otherwise expressly provided, in order to simplify the taxpayer's filing of returns, reduce the taxpayer's accounting burdens, and facilitate the collection and administration of these taxes." (32 V.S.A. §5820(a)).

[3] 32 V.S.A. §5833(a) provides, in part:

". . . If the income of a taxable corporation is derived from any trade, business or activity conducted both within and without this state, the amount of the corporation's Vermont net income which shall be apportioned to this state, so as to allocate to this state a fair and equitable portion of that income, shall be determined by multiplying that Vermont net income by the arithmetic average of the following factors:

(1) The average of the value of all the real and tangible property within this state (A) at the beginning of the taxable year and

(*Footnote continued*)

If it is established that the formula does not apportion to Vermont that share of a taxable corporation's net income which fairly represents the extent of its business activities in Vermont, then the Commissioner of Taxes (the "Commissioner") is directed to make such modifications as are necessary to achieve such fair apportionment.[4] Accordingly, both the application of the appor-

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(B) at the end of the taxable year, expressed as a percentage of all such property both within and without this state;

(2) The total wages, salaries, and other personal service compensation paid during the taxable year to employees within this state, expressed as a percentage of all such compensation paid whether within or without this state;

(3) The gross sales, or charges for services performed, within this state, expressed as a percentage of such sales or charges whether within or without this state."

[4] 32 V.S.A. §5833(b) provides, in part:

". . . If the application of the provisions of this section does not fairly represent the extent of the business activities of a corporation within this state, the corporation may petition for, or the commissioner may require, with respect to all or any part of the corporation's business activity, if reasonable:

(1) Separate accounting;

(2) The exclusion or modification of either [*sic*] or both [*sic*] of the factors;

(3) The inclusion of one or more additional factors which will fairly represent the corporation's business activity in this state; or

(4) The employment of any other method to effectuate an equitable allocation and apportionment of the corporation's income."

While the Vermont definition of net income makes no distinction between business and nonbusiness income, in the proper case, that distinction could be made by the Commissioner under his power to modify the apportionment to insure that it fairly represents the extent of business activities in Vermont. (Cf. UDITPA § 1(a), 1(e), 4 and 7, Regulations § IV.1.(c).(4). See also ASARCO v. Idaho, No. 78-1839)

tionment formula and the Commissioner's power to modify that formula assure that the Vermont tax is applied only to that share of a taxable corporation's net income which fairly represents the extent of its business activities in Vermont.

II. *The Vermont Tax Returns Filed by Mobil*

In 1970, 1971 and 1972, Mobil Oil Corporation ("Mobil") produced, transported, refined, distributed and sold petroleum and petroleum products, including chemicals, and held stocks in related operating subsidiaries and affiliates. Mobil's income for those years included income from Mobil's activities in Vermont and elsewhere and included dividends from operating subsidiaries and affiliates. For each of those years, Mobil filed a Vermont corporate income tax return on which it reported its federal taxable income and its Vermont and worldwide payroll, property and sales factors.[5] Rather than report its federal taxable income as its Vermont net income, as required by the Vermont Statutes, Mobil calculated its net income, before apportionment, by subtracting from federal taxable income, all income received as dividends.[6] By thus reducing federal taxable income and, consequently, net income before apportionment, Mobil was able to report no taxable income to Vermont for two of the three years in question.

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[5] Mobil's Vermont tax returns are reproduced in the single Appendix filed by the parties (hereinafter referred to as "App."), at pages A33, A47 and A61, respectively. A synopsis of the information contained in those returns, in table form, is annexed to this Brief as Appendix I.

[6] In addition, Mobil deducted interest and foreign taxes, claims which it has abandoned on this appeal. The calculations as reported by Mobil were as follows:

(*Footnote continued*)

The Vermont Department of Taxes recalculated Mobil's tax liability in accord with the Vermont Statutes using federal taxable income as Vermont net income, before apportionment, and determining apportioned net income and the Vermont tax accordingly. The Department of Taxes assessed Mobil for the resulting tax deficiency.

For the years in question, Mobil reported gross income of $2,107,519,818.23, $2,306,420,151.25 and $2,444,866,994.00, and total deductions of $1,786,558,689.94, $1,893,136,692.06 and $2,065,517,997.33, respectively. (Forms 1120, lines 11 and 27, App., at pages A38, A39, A52, A53, A66 and A67, respectively). By reducing Vermont net income, before apportionment by "non-apportionable" dividend income, Mobil subtracted from "apportionable" income, all deductions. In other words, Mobil deducted from the income of its integrated petroleum business, after it excluded dividend income, the costs and expenses attributable to its stockholdings. As a result of the exclusion of so-called "non-apportionable" income, and the allocation of all deductible costs and expenses to remaining gross income, Mobil created and reported for Vermont tax purposes, net operating losses for two of the three years at issue.

Year	*1970*	*1971*	*1972*
U.S. Taxable Income	$220,035,244	$308,253,570	$232,825,728
Non-Apportionable Income			
Dividends	174,211,073	282,817,008	280,623,403
Interest	10,520,792	12,609,826	3,905,208
Foreign Taxes	12,221,476	34,659,576	38,260,249
Subtotal	196,953,342	330,086,410	322,788,861
Vermont Net Income, Before Apportionment	$ 23,081,901	($21,832,840)	($89,963,133)

(App., at pages A37, A51 and A65, respectively).

III. *The Facts*

During the course of the Vermont tax proceedings Mobil submitted a "stipulation" to the Commissioner, who rejected it as ". . . the facts that support your arguments alone." (Transcript of Commissioner's Hearing of November 8, 1973, App., at page A13). It is this selective and artfully-phrased statement which Mobil submits to this Court as a "Stipulation."[7] In view of the carte blanche Mobil had to present those facts which supported its arguments, it is curious that the Record is so sparse. Mobil alleged only two relevant facts in its Statement: first, that Mobil was engaged in the petroleum business in the United States, including exploration, production, refining, transportation, distribution and sale of petroleum and petroleum products; and second, that Mobil markets petroleum products and related products in Vermont. The Statement also asserts that Mobil's management and custody of the stocks of its operating subsidiaries and affiliates took place outside Vermont, but, as will be shown, this assertion is not relevant to the issues here presented. (Statement, paragraphs (6), (9) and (11), App., at pages A81, A82 and A83, respectively).

IV. *Proceedings Below*

Mobil appealed the assessed tax deficiencies to the Commissioner and presented, in support of its appeal, a variety of arguments raising issues of statutory interpretation and constitutional limitations. In addition, Mobil petitioned the Commissioner to modify the apportionment of its net income to Vermont pursuant to his authority under 32 V.S.A. § 5833(b). The modifications Mobil sought were the exclusion of its income received as dividends from net income, before apportionment, or modification

[7] Mobil's proposed stipulation is hereinafter referred to as Mobil's "Statement."

of the apportionment factors to achieve the same Vermont tax result.[8]

The Commissioner rejected Mobil's statutory interpretation and claims of constitutional limitations and denied Mobil's petition for modification.[9] In support of his determination, the Commissioner quoted, with approval, from an opinion of the Vermont Supreme Court, that:

> " '. . . the realistic value of the exercise of a franchise in a particular state is enhanced and contributed to by the worth or income of the entire enterprise.' . . . Typically, this approach is followed where there is a unity of use and management of the enterprise being taxed." (*F.W. Woolworth Co. v. Commissioner of Taxes*, 130 Vt. 544, 549, 298 A.2d 839 [1972]).

Mobil timely and properly appealed the Commissioner's determination to the Washington Superior Court, which sustained the Commissioner's determination on all issues except the constitutional limitations of the Commerce Clause. On that issue the Superior Court held that:

> "However, because the commercial domicile of plaintiff does have the authority to tax investment dividends and interest without apportionment; because the capacity to tax, and

[8] The legal argument presented in support of Mobil's petition for modification appears in the Transcript of Commissioner's Hearing of November 8, 1973. (App., at pages A11, A25 and A26.)

[9] The Commissioner, in his determination, specifically rejected both alternatives requested in Mobil's petition for modification. (Page 4a of the Appellant's Jurisdictional Statement (hereinafter referred to as "JS. App."), paragraphs A. and B., and page 12a and 13a, paragraphs 1 and 2). The Commissioner did grant Mobil's petition to modify in another respect—gross up of dividends—which is not an issue before this Court. (JS. App., page 13a, paragraph 5).

not the actual imposition of same, is the test, such income could be the subject of prohibitive multiple taxation by inclusion in the Vermont apportionment base." (Unreported opinion, J.S. App., at page 16a).

The Commissioner of Taxes timely and properly appealed the decision of the Washington Superior Court to the Vermont Supreme Court. That Court considered the single question:

". . . Does Vermont's application of its apportioned net income tax to the investment income in issue constitute multiple taxation prohibited by the Commerce Clause?" (*Mobil Oil Corp. v. Commissioner of Taxes*, 136 Vt. 545, 548, 394 A.2d 1147 [1978] (JS. App., at page 22a)).

The Vermont Supreme Court held:

"The burden is upon the taxpayer to demonstrate a risk of multiple taxation. (Citations omitted.)

Mobil in the case at bar has not established that its commercial domicile can tax the investment income of its domiciliary corporation without apportionment." (*Id.* at page 548 and page 23a, respectively).

As to whether the risk, as opposed to actual multiple taxation, is the proper constitutional test, the Court said:

"We do not decide this issue in the case at bar since Mobil has failed to establish on the record that New York has the power to tax investment income without apportionment, and hence no risk of multiple taxation is here shown." (*Id.* at page 549 and page 24a, respectively).

While the issue presented in this appeal is a narrow one, the Court's decision on Mobil's claims has potentially far-reaching consequences. In recognition of this fact, Vermont has consented to the filing of briefs by Standard Oil Company of California,

the State of Illinois, and the Multistate Tax Commission, as *amici curiae*, in support of the Appellee.

Statement of the Issue

Does the Constitution permit a state to impose a tax on the net income of a corporation, which regularly and continuously engages in substantial business activities in that state, fairly apportioned to reflect the extent of such business activities where:

1. The corporation receives virtually all of its net income in the form of dividends from operating subsidiaries and affiliates; and

2. The corporation neither alleges nor proves that its operating subsidiaries and affiliates do not comprise integral parts of its worldwide, integrated business, a part of which is conducted in the taxing state?

Summary of the Arguments Presented

I. Mobil has not met its required burden of proving by clear and cogent evidence that the Vermont tax was imposed on extraterritorial values or created a prohibited tax burden on interstate or foreign commerce.

II. In the context of a tax on apportioned net income, the geographical location of income-producing property or activities is not relevant to the determination of tax base, before apportionment. Whether a tax is valid depends on whether the formula apportions to the taxing state that share of a taxpayer's net income fairly attributable to business activities in that state. Mobil has not proved that Vermont's apportionment formula, as applied to its net income, including income received as dividends, does not allocate to Vermont that por-

tion of its net income fairly attributable to its business activities in Vermont.

Mobil's nexus with Vermont was substantial, and the Vermont tax assessed bears a fair relationship to the value of the protections, opportunities and benefits provided by Vermont. Accordingly, the Vermont tax on apportioned net income satisfies the requirements of the Due Process and Commerce Clauses.

III. Mobil has failed to show either the existence of a risk or the fact of constitutionally prohibited multiple taxation.

Mobil's claim that New York, the state of its commercial domicile, has the constitutional power to tax, without apportionment, all income received as dividends, is not supported by the decisions of this Court or the economic realities of interstate commerce.

IV. Mobil's claim that this Court's decision in *Japan Line, Ltd. v. County of Los Angeles* (47 U.S.L.W. 4477 [April 30, 1979]) is relevant to the issue here presented represents an unwarranted extension and interpretation of that decision.

Argument

I. *Mobil has Failed to Present a Factual Record Sufficient to Sustain its Burden of Proof.*

This Court has clearly stated and consistently required that:

"One who attacks a formula of apportionment carries a distinct burden of showing by 'clear and cogent evidence' that it results in extraterritorial values being taxed. *See Norfolk & Western Ry. Co. v. North Carolina,* 297 U.S. 682, 688." (*Butler Brothers v. McColgan,* 315 U.S. 501, 507, [1942].

See also Underwood Typewriter Co. v. Chamberlain, 254 U.S. 113 [1920]).

In *Moorman Manufacturing Co. v. Bair* (437 U.S. 267, 274 [1978], this Court confirmed:

". . . that the States have wide latitude in the selection of apportionment formulas and that a formula-produced assessment will only be disturbed when the taxpayer has proved by 'clear and cogent evidence' that the income attributed to the State is in fact 'out of all appropriate proportion to the business transacted . . . in that State,' (citation omitted), or has 'led to a grossly distorted result.' (citation omitted)."

Mobil asks this Court to void the Vermont tax on apportioned net income but has failed to present a factual record on which such relief can be granted. Mobil has neither claimed nor proved that its net income apportioned to Vermont was out of proportion to its business activities in Vermont. Having failed to prove the amount of its net income attributable to business activities in Vermont for the years in question, Mobil's claim of extraterritorial taxation is without foundation and foreclosed by prior decisions of this Court. Having failed to prove either actual multiple taxation or a substantial risk of multiple taxation, Mobil's claim that the tax in question results in multiple burdens prohibited by the Commerce Clause is purely speculative. Therefore, it is respectfully suggested, that the Record presented does not support Mobil's claim for relief from this Court.

II. *Vermont's Apportioned Net Income Tax Satisfies the Requirements of the Due Process Clause because Vermont has Nexus with Mobil and Mobil has failed to Show that its*

Income Taxed is Grossly Disproportionate to its Business Activities in the State.[10]

Properly apportioned state taxes on the income of multistate corporations have been upheld by this Court in spite of the fact that they may, in some way, burden interstate commerce. As this Court said in *Northwestern States Portland Cement Co. v. Minnesota* (358 U.S. 450, 461, 462 [1959]):

> ". . . it is axiomatic that the founders did not intend to immunize such commerce from carrying its fair share of the costs of the state government in return for the benefits it derives from within the State."

The constitutional validity of a state tax on apportioned net income is determined by whether the formula apportions to the taxing state that share of a taxpayer's net income fairly attributable to business activities in that state. The rationale for this constitutional limitation is that:

> "Logically it is impossible, when the tax is fairly apportioned, to have the same income taxed twice." (*Id.*, at page 462).

A tax on net income is a tax on a stated amount of dollars which are indistinguishable as to the location of the income-producing property or activity. The appropriate share of a business' net income which may properly be taxed by a particular state is determined by apportionment. As stated by this Court in *Moorman* (*supra*, at page 273), a tax on apportioned net income:

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[10] Because Mobil failed to properly raise, brief or argue before the Vermont Supreme Court any claim under the Due Process Clause, the Commissioner contends that Mobil has not properly raised before this Court any issue under that Clause. (See Motion to Dismiss or Affirm, at pages 7 through 12).

> ". . . does not purport to identify the precise geographical source of a corporation's profits; rather, it is employed as a rough approximation of a corporation's income that is reasonably related to the activities conducted within the taxing State."

Mobil's counsel, an adjunct professor-of-law at New York University and an authority on the subject of state taxation, described the development of the concept of apportionment in the following terms:

> "It is important to realize that apportionment by formula grew out of necessity; it grew out of the fact that no one has ever been able to develop any kind of satisfactory method of accounting for measuring the legitimate claims of the various States to tax the income which is reflected in a series of interdependent basic operating transactions of an enterprise, such as manufacturing, producing, mining, or timbering in one State and selling in another, or buying in one State and selling in another." (Statement of Professor Hellerstein at Hearings before the Subcommittee on State Taxation of Interstate Commerce of the Committee on Finance, United States Senate, 93d Congress, 1st Session, 151 [1973]).

Mobil argues, at page 9 of its Brief, that because it managed and held the stocks of its operating subsidiaries and affiliates outside the state, Vermont lacked the nexus required by the Due Process Clause to tax the dividends produced by those stocks and that, therefore, Vermont must exclude from its net income, before apportionment, all income received as dividends.

In arguing that the property or activities which produce component items of income, before apportionment, must be physically located in the taxing state, Mobil ignores the underlying rationale recognized by this Court that apportionment is an alternative to separate accounting by geographical location. Because Mobil re-

ceived virtually all of its net income in the form of dividends, the effect of Mobil's argument is to reduce to a nominal amount (zero in two of the three years in question) Vermont's tax base, before apportionment.

Conceptually, Mobil's argument is analogous to the taxpayers' arguments in *Bass, Ratcliff & Gretton v. Tax Commission* (266 U.S. 271 [1924]) and *Butler Brothers v. McColgan* (*supra*). In those cases, the taxpayers argued that, by their methods of separate accounting, their business operations in the taxing states produced net losses. In this case, Mobil, although never asserting that its business activities in Vermont were not profitable if isolated by separate accounting, attributes to Vermont net losses resulting from unspecified business activities in unspecified locations by its own method of separate accounting (excluding only income received as dividends from tax base). For those same years Mobil reported substantial federal taxable income without identifying the sources of its profits.[11] In *Butler Brothers v. McColgan*, this Court responded to the taxpayer's attempt to avoid California's income tax by attributing no net income to California, saying:

> "A particular accounting system, though useful or necessary as a business aide, may not fit the different requirements when a state seeks to tax values created by business within its borders. (Citations omitted.) That may be due to the fact, as

[11] Actually, the net losses are artificially produced by Mobil's system of accounting. For example, in 1972, 121% of Mobil's taxable income was received in the form of dividends paid by companies whose value represented 48% of Mobil's net worth. From those figures it would appear that Mobil's so-called operating business, representing 52% of its net worth, operated at a substantial loss. Clearly, this method of accounting, while perhaps useful for some purposes, lacks reality. (Statement, paragraphs (13) and (16), App., at pages A83 and A84).

> stated by Mr. Justice Brandeis in *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113, 121, 41 S. Ct. 45, that a state in attempting to place upon a business extending into several states 'its fair share of the burden of taxation' is 'faced with the impossibility of allocating specifically the profits earned by the processes conducted within its borders.' . . . the fact of the matter is that appellant has not shown the precise sources of its net income of $1,149,677. If factors which are responsible for that net income are present in other States but are not present in California, they have not been revealed. At least in absence of that proof, California was justified in assuming that the San Francisco branch contributed its aliquot share to the advantages of centralized management of this unitary enterprise and to the net income earned. . . . and no showing has been made that income unconnected with the unitary business has been used in the formula."

(*See also Bass, Ratcliff & Gretton v. Tax Commission, supra; Underwood Typewriter Co. v. Chamberlain, supra*).

In *Moorman* (*supra*), the taxpayer argued that the Iowa tax on apportioned net income was imposed on extraterritorial values. The Court observed, at page 272:

> "This argument rests on two premises: first, that appellant's Illinois operations were responsible for some of the profits generated by sales in Iowa; and, *second, that a formula that reaches any income not in fact earned within the borders of the taxing State violates due process. The first premise is speculative and the second is foreclosed by prior decisions of this Court.*" (Emphases added.)

It is respectfully suggested that Mobil's Due Process claim is foreclosed by *Moorman* and prior decisions of this Court.

Mobil's argument that the income it received as dividends cannot be included in Vermont net income, before apportionment, appears to be based on the unsupported premise that its stockholdings were somehow separate from and unrelated to its worldwide, integrated petroleum business conducted, in part, in Vermont. Mobil would have this Court believe that because it holds stocks of its operating subsidiaries and affiliates outside Vermont, it is therefore a disinterested investor whose stockholdings are a separate business unrelated to its worldwide, integrated petroleum business. Even if Mobil's argument was sound that income source is relevant to the base of an apportioned net income tax, the premise upon which it makes that argument is not. Mobil has neither claimed nor proved that its operating subsidiaries and affiliates and income received as dividends were unrelated to its worldwide, integrated petroleum business. Mobil alleges only that the business activities of its operating subsidiaries and affiliates do not take place in Vermont, without revealing the nature of such activities, where they do take place, or their relationship to other components of Mobil's integrated petroleum business.

Reasonable inferences from the Record make it apparent that the dividends at issue, in fact, were derived from stockholdings in operating businesses integrally related to Mobil's petroleum business. For example, Mobil's stockholdings in ARAMCO, Mobil Marine Transportation Limited, Mobil Oil Iran with Limited Liability and Pegasus Overseas Limited could hardly be considered disinterested investments unrelated to Mobil's need to secure adequate supplies of crude oil, transportation and refining capacity and markets. The Record establishes that dividends from these four corporations, three of which are wholly-owned subsidiaries, equal approximately 90% of the income here at issue. (App., at pages A75 and A76).[12] The fact that Mobil has chosen to conduct certain of its integrated business activities through subsidiaries and affiliates, rather than through operating divisions, should not limit Vermont's right to impose a tax on Mobil's net income fairly apportioned to business activities in Vermont.[13]

With regard to the relationship between Mobil's income received as dividends and its financial operations, Mobil has not revealed how that income was used. Mobil has not disassociated such income from use to finance daily operations in Vermont, to purchase Vermont property, to pay Vermont wages, to purchase or finance the petroleum products marketed in Vermont or to otherwise, directly or indirectly, benefit its business activities in Vermont. Nor has Mobil revealed the source of the

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[12] In addition to claiming lack of nexus between Vermont and its stockholdings, Mobil urges this Court to attribute significance to its claim that there was no nexus between Vermont and the underlying business activities and earnings of its operating subsidiaries and affiliates. By this argument, Mobil erroneously equates the income-producing activities of its operating subsidiaries and affiliates with the income received by it as dividends paid on their stocks.

[13] The integral nature of Mobil's operating subsidiaries and affiliates to its integrated worldwide petroleum business is apparent from the testimony of William P. Tavoulareas, President, Mobil Oil Corporation, before the Subcommittee on Anti-Trust and Monopoly of the Committee on the Judiciary of the United States Senate on January 21, 1976:

> ". . . It is a fact that . . . . this [development of prosperity and power] was made possible by an international oil industry which produced, refined, and marketed the oil, using a tremendously complex logistics system which got the right crude oil or product to the right customer at the right time.
>
> . . .
>
> Let me talk briefly now about the function of size in our international operations—again as this relates to the U.S. consumer. Look back at the 1973–1974 embargo period. When the Arab nations cut

(Footnote continued)

funds with which it purchased the stocks in its operating subsidiaries and affiliates.[14]

Furthermore, to the extent that Mobil borrows operating funds and seeks funds in the debt and equity capital markets, Mobil presents itself to commercial lenders and bond and stock market investors as a fully integrated, worldwide petroleum company. Finally, the Record makes no mention of where and by whom the products marketed in Vermont were produced, refined or transported.

In addition to proposing an inappropriate constitutional test and failing to provide a factual record which supports its claim of extraterritorial taxation by clear and cogent evidence as required, Mobil has failed to account appropriately for its gross income, costs and deductions. Mobil has not identified on the Record, by the location of the income-producing property or activity, either gross receipts or deductible costs and expenses. Therefore, it is not possible, on the facts presented, to compute net income for property or activities located in a particular state. While Mobil has separately accounted for its income received as dividends, it has not separately accounted for the costs and expenses attributable to its stockholdings. Those costs and expenses were deducted as ordinary and necessary business expenses in computing Mobil's federal taxable income and, accordingly, Vermont net income before apportionment. Those costs and expenses, to the extent they included property and payroll, were included in the denominator of those factors in the Vermont apportionment formula.

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off oil supplies to the United States, the large oil companies utilized their worldwide logistics capability to move more non-Arab oil into the United States and move Arab oil to countries which were not embargoed."

[14] From the information Mobil has provided, the source of such funds could have been the profits earned by Mobil's Vermont business activities.

The implications of the constitutional test proposed by Mobil are enormous. That test, if accepted and applied consistently to other component items of income, would exclude from a state's tax base, Mobil's gross receipts from exploration, production, refining, transportation and marketing activities which take place outside that state. While the gross receipts from those activities would be excluded from tax base, before apportionment, the costs and expenses incurred in those activities would, nonetheless, under Mobil's theory, be deducted in computing federal taxable income and, consequently, from tax base, before apportionment.

Mobil's business activities in Vermont during the three years in question resulted in total Vermont sales of $27,319,578 and a total Vermont payroll of $736,068. During this period, Mobil's total property increased from $3,930,100 to $8,236,792. Clearly, these activities establish both a substantial nexus between Mobil and Vermont, and a substantial demand by Mobil for protections, opportunities and benefits provided by Vermont. Nonetheless, by the simple expedient of excluding income received as dividends from Vermont net income, before apportionment, Mobil artificially created, for Vermont tax purposes, substantial net losses without any demonstration of the actual profitability of its business activities in Vermont.

Instead of a total tax base for 1970, 1971, and 1972 of $1,273,646, Mobil reported a negative tax base of $173,648. The tax base reported by Mobil for each of the years in question would result in total tax payments of only $1,178 for Vermont's privileges, protections and opportunities instead of taxes totalling $76,417, computed on an average of .0016727 of Mobil's federal taxable income. If Mobil's Vermont sales had a 4.7% profit margin, Mobil's actual profits in Vermont would have exceeded the net income apportioned to Vermont by the formula. By con-

trast, Mobil's proposed method of accounting would result in those sales producing a substantial net loss. It is hardly credible that the increase in Mobil's business in Vermont during the period in question, both absolutely and as a percentage of its worldwide business, would have occurred unless Mobil's Vermont operations were, in fact, very profitable.

Clearly, an apportioned net income tax if restricted to a tax base limited to income derived from sources within the taxing state, would bear no fair relationship to the protections, opportunities and benefits provided by the taxing state or to the profits generated from business conducted in that state. Surely a state which provided the opportunities of a market which produced more than $27 million in Vermont sales for Mobil; which provided protections for Mobil's property which totalled, in 1972, $8.2 million; and which provided services which supported Mobil's payroll of more than $736,000, has a legitimate claim to fair compensation.

III. *Vermont's Apportioned Net Income Tax Satisfies the Requirements of the Commerce Clause because Mobil Is neither Subjected to a Substantial Risk nor the Actuality of Multiple Taxation.*

Mobil argues that Vermont's tax on apportioned net income contravenes the Commerce Clause because it creates an impermissible risk of multiple taxation of its interstate and foreign commerce. The risk asserted is the possibility that more than 100% of Mobil's income received as dividends will be taxed by various states as a result of diverse apportionment formulas or, alternatively, that New York, as the state of Mobil's commercial domicile, has the constiutional authority to tax such income without apportionment. However described, the issue raised is one of fair apportionment, and Mobil's claim is foreclosed by this Court's decision in *Moorman* (*supra*).

In *Moorman*, the taxpayer contended that the Iowa single-factor formula apportioned to Iowa income which was also taxed by Illinois. Therefore, the taxpayer argued, the Iowa tax created an impermissible multiple burden in violation of the Commerce Clause. The Court first analyzed the facts presented, finding that:

> "this record does not establish the essential factual predicate for a claim of duplicative taxation. Appellant's net income during the years in question was approximately $9 million. Since appellant did not prove the portion derived from sales to Iowa customers, rather than sales to customers in other States, we do not know whether Illinois and Iowa together imposed a tax on more than 100% of the relevant net income." (*Id.*, at page 276).

The Court required a showing of *actual multiple taxation*, and finding the taxpayer's evidence deficient, held that the existence of multiple burdens was speculative.

Mobil does not claim actual multiple taxation and the Record contains no real evidence of any substantial risk of multiple taxation. New York does not tax dividends from Mobil's subsidiaries, which represent the vast majority of the dividends here at issue, and taxes only a very small portion of the dividends from non-subsidiaries. (JS. App., page 39a). Since Mobil cannot even assert, much less prove, actual double taxation in this case, under *Moorman*, this ends the inquiry and the existence of an impermissible burden is speculative.[15]

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[15]As to the substantiality of the risk Mobil faces, the economic realities of taxation by states of commercial domicile are the subject of an excellent analysis which concludes:

> "Major domiciliary states have found that ultimately it is more profitable to lure interstate businesses to settle in the state than to tax their dividend income. As an incentive for corporations to locate within them, these states deliberately treat such income specially."

(*Footnote continued*)

The *Moorman* decision was not the first time the Court required an essential "factual predicate" for a claim of duplicative taxation. In *Northwestern States* (*supra*), the Court said, at page 462:

> "One of the 'realities' raised by the parties is the possibility of a multiple burden resulting from the exaction in question. The answer is that none is shown to exist here. . . . there is nothing to show that multiple taxation is present. We cannot deal in abstractions."

In *Standard Pressed Steel Co. v. Department of Revenue of Washington* (419 U.S. 560 [1975]), this Court considered a challenge to the Washington gross receipts tax (a tax inherently more burdensome than the tax here at issue) based on the taxpayer's claim that the tax created a risk of multiple taxation. In *Standard*, as in this case, it was conceded that actual multiple taxation did not exist, but argued that the risk that another state might tax the same tax base created an impermissible risk of multiple burden. In this case, Mobil argues that New York might impose an unapportioned tax on 100% of its dividends which are included in Vermont's tax base before apportionment. In *Standard*, this Court held:

> "We noted in *General Motors* that a vice in a tax on gross receipts of a corporation doing an interstate business is the risk of multiple taxation; but that the burden is on the taxpayer to demonstrate it. . . . The corporation made no such showing there. Nor is any effort made to establish it here." (*Id.*, at page 563).

State Taxation of Interstate Businesses and the Multistate Tax Compact: The Search for a Delicate Uniformity, Columbia Journal of Law and Social Problems, 231 (1975). Cited in Footnote 13, at page 278 of *Moorman*.

Even if the constitutional test is a risk of multiple taxation, the possibility that another state might at some time in the future impose a tax creating a multiple burden was found insufficient under *Standard* to establish a violation of the Commerce Clause. Accordingly, Mobil, like Standard, has failed to establish the essential factual predicate for a claim of multiple taxation. Whether the requirement is a showing of a substantial risk, or actual multiple taxation, Mobil has failed to establish either, and the Record on which Mobil bases its claim is insufficient.

Not only does the possibility that New York might, in the future, attempt to tax 100% of Mobil's dividends fail to establish an unconstitutional risk of double taxation, Mobil's argument that the Constitution grants to states of commercial domicile the power to tax, without apportionment, all income received as dividends lacks support in the decisions of this Court and the economic realities of interstate commerce.

Mobil's argument that the doctrine of *mobilia seguuntur personam* requires allocation of 100% of dividend income to the state of commercial domicile exalts fiction over reality. This medieval maxim, with no unequivocal constitutional source, was developed in early inheritance and property tax cases. Its application, in the context of a tax on fairly apportioned net income, has no discernable merit. The doctrine of fair apportionment proceeds from the principle that a state which provides services, opportunities and protections has a right to impose taxes which bear a fair relationship to the value of the benefits provided. The *mobilia* doctrine would allocate all income from intangible property to a single state based on a unilateral business choice of commercial domicile, without regard to the extent of business activities in other states, or the privileges, opportunities and protections provided by those states. In the critical area of state taxa-

tion of net income, the anachronistic and economically unrealistic *mobilia* doctrine should yield to a rule of fair apportionment.[16]

The so-called fiscal policy considerations advanced by Mobil in support of the *mobilia* doctrine, applied to the facts in this case, support the choice of fair apportionment rather than 100% allocation to New York. Mobil has not alleged or proved any relationship between the location of its management and custodial activities and the State of New York nor has it shown that New York provided any benefits or protections or incurred any social costs in connection with its stockholdings. Vermont, on the other hand, provided significant markets—a critical element in Mobil's integrated worldwide petroleum business. The *mobilia* doctrine would grant to New York the power to tax solely because it was selected by Mobil as its commercial domicile, and deny Vermont the ability to claim fair compensation for the opportunities, privileges and protections provided. Surely, the Constitution does not require or support such a result.

IV. *This Court's Decision in* Japan Line, Ltd., *Is Not Precedent for Its Decision on Mobil's Claims.*

Finally, with its risk of multiple taxation theory foreclosed by *Moorman*, Mobil argues for a more restrictive test because the component items of net income at issue were, it asserts, "foreign source" dividends. Citing *Japan Line* (*supra*), as precedent, Mobil asks this Court to declare that the risk of taxation of its dividends by more than one state, which may result from diverse methods of apportionment, is prohibited by the Commerce Clause because some of its dividends were paid by foreign operating subsidiaries and affiliates.

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[16] Mr. Justice Stewart's concurring opinion in *California v. Texas*, (437 U.S. 601 [1978]) suggests that the Court if ever faced with multiple taxation by the states arising from multiple state contacts would resolve the conflict by some method of apportionment rather than resort to a "single 'correct' answer under state common law." (*Id.* at page 613).

Mobil asserts that:

> "Although there are factual differences between *Japan Line* and the case at bar, none warrants a different result." (Appellant's Brief, at page 24).

In fact, the cases differ in so many significant respects that the issues and considerations raised in *Japan Line* bear no resemblance to those here presented. A review of only a few of the significant differences should suffice to prove this point.

First, as previously stated, only Mobil's net income apportioned to its activities in Vermont was subject to the Vermont tax. Mobil has neither asserted nor proved that its net income apportioned to Vermont had any relationship with foreign commerce. The only connection with foreign commerce on the Record is that Mobil's operating subsidiaries and affiliates are alleged to conduct business outside the United States. By so arguing, Mobil confuses its business activities with the business activities of its operating affiliates and subsidiaries.

A second significant difference is that in *Japan Line*, the tax at issue was an ad valorem property tax. The constitutional standards applied to such taxes are based on entirely different considerations from those applicable to a tax on apportioned net income.

A third significant difference is that in *Japan Line*, actual multiple taxation by a state and a foreign nation was found to exist. Mobil admits that Vermont's apportioned net income tax creates no duplicative taxation of its net income but asserts a mere speculative risk of possible multiple burden. A critical element in this Court's analysis and decision in *Japan Line* was the fact that a foreign sovereign had imposed a tax on the property at issue. Because the Court lacks the power to limit taxa-

tion by foreign nations, it lacked the power to correct unfair apportionment which might exist. The risk of multiple taxation asserted here is the risk that more than 100% of Mobil's net income will be exposed to taxation by overlapping state formulas. Accordingly, all taxing authorities involved are subject to the Court's jurisdiction. To suggest, as Mobil does, that this is a distinction without difference, is preposterous. Obviously it was to precisely that overlap that this Court referred when it said:

> "Errors of apportionment that may lead to multiple burdens may be corrected when they occur." (*Department of Revenue of Washington v. Association of Washington Stevedoring Companies*, 435 U.S. 734 [1978]).

Conclusion

The order of the Vermont Supreme Court should be affirmed.

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Respectfully submitted,

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Appendix I

	1970	1971	1972
1. Federal Taxable Income	$220,035,244	$308,253,570	$232,825,728
2. Vermont Sales	8,554,200	9,175,931	9,589,447
3. Vermont Property	3,930,100	6,707,534	8,236,792
4. Vermont Payroll	236,553	244,577	254,938
5. Vermont Sales as a Percentage of Worldwide Sales	0.239134%	0.235924%	0.236787%
6. Vermont Property as a Percentage of Worldwide Property	0.136845%	0.223887%	0.250225%
7. Vermont Payroll as a Percentage of Worldwide Payroll	0.062118%	0.061131%	0.059440%
8. Vermont Apportionment Percentage	0.146032%	0.173647%	0.182151%
9. Federal Taxable Income Received in the Form of Dividends	174,211,073	282,817,008	280,623,403
10. *Percentage of Federal Taxable Income Received in the Form of Dividends	79%	92%	121%
11. Net Income Apportioned to Vermont Excluding Income Received in the Form of Dividends	30,361	(40,058)	(163,951)
12. *Net Income Apportioned to Vermont Including Income Received in the Form of Dividends	317,976	532,592	423,078
13. Vermont Tax Excluding Income Received in the Form of Dividends	1,821	25	25
14. *Vermont Tax Including Income Received in the Form of Dividends	19,078	31,955	25,384

* Not reported by Mobil on Vermont tax returns, as filed, calculated on the basis of information contained in those returns.